BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

DOCKET NO. UE-011514

DIRECT TESTIMONY OF RONALD L. MCKENZIE

REPRESENTING AVISTA CORPORATION

Q. Please state your name, business address and present position with Avista Corporation ("Avista" or "Company").

A. My name is Ronald L. McKenzie and my business address is East 1411 Mission Avenue, Spokane, Washington. I am employed by Avista as a Senior Rate Accountant.

Q. Would you briefly describe your educational background?

A. I was graduated from Eastern Washington University in 1973 with a Bachelor of Arts degree in Business Administration majoring in accounting. I obtained a Master of Business Administration Degree from Eastern Washington University in 1989. I have attended several utility accounting and ratemaking courses and workshops.

Q. How long have you been employed by Avista and what are your present duties?

A. I was first employed by Avista in September 1974. My present duties include preparing data related to regulatory matters and presenting testimony before regulatory commissions.

Q. Have you previously testified before this Commission?

A. Yes. I have testified before this Commission in several prior proceedings.

Q. What is the scope of your testimony in this proceeding?

A. My testimony addresses the accounting associated with the power cost deferrals authorized by the Commission. I also explain the interest calculation, the monthly reports that are filed with the Commission, and the retail revenue component of the power cost deferral mechanism.

Q. Would you please describe the accounting associated with the Company's deferral mechanism?

A. Yes. Company witness, Mr. Johnson, discusses in his direct testimony the procedure used to calculate the monthly variations between actual and authorized power supply revenues and expenses that are deferred. When actual net power supply costs have been greater than authorized costs, entries have been made to record the difference by crediting Account 557.28 - Other Power Supply Expenses, thereby decreasing recorded power supply expenses, and debiting Account 186.28 - Miscellaneous Deferred Debits. If actual net power supply costs are less than authorized costs in a given month, an entry would be made to record the difference by debiting Account 557.28 - Other Power Supply Expenses, thereby increasing recorded power supply expenses, and crediting Account 186.28 - Miscellaneous Deferred Debits. The accumulated debit balance in Account 186.28 represents a surcharge balance.

Q. What is the balance in Account 186.28 at September 30, 2001 and on what amount is the Company requesting a determination of prudence and recoverability in this case?

A. The debit balance in the deferral account at September 30, 2001 is $199,658,987. The Company is proposing to address the prudence and recoverability of fixed costs associated with natural gas and diesel-fueled small generation projects in the upcoming general rate case. The net amount to be addressed in this case is $198,472,123 as shown below:

Balance of deferred costs at 9/30/01	$199,658,987
Less small generation fixed costs	-1,186,864
Net to be addressed in this case	$198,472,123

Q. How does the Company record interest on the balance in Account 186.28?

A. Interest is calculated on the average of the beginning and ending month balances in Account 186.28 net of deferred federal income tax. The interest rate used is 9.03%, the rate of return authorized in the Company's last general rate case, Docket No. UE-991606. Interest is compounded monthly since the interest rate I s applied to the average monthly balance in Account 186.28, which includes interest accrued from previous months. Monthly compounding is consistent with the method used in the recording of interest on the Company's purchase gas cost deferral accounts. The monthly compounding procedure for deferred gas costs has been in place and has been included in purchase gas rate adjustments approved by the Commission since at least 1992. Monthly compounding was also used in computing interest on the portion of the gain on the sale of the Centralia that was passed on to electric customers.

Q. What amount of interest is included in the deferral balance at September 30, 2001?

A. The interest included in the deferral balance at September 30, 2001 amounts to $4,947,637.

Q. What reports has the Company submitted to the Commission?

A. The Company has submitted monthly reports to the Commission, which have included the monthly power cost deferral journal entries together with backup workpapers and other supporting documentation.

Q. How are income taxes accounted for under the deferred power cost mechanism?

A. The power cost deferral entries and amortization entries are not included in the determination of taxable income for federal income tax purposes. Therefore, deferred federal income taxes are recorded. Account 283.28 – Accumulated Deferred Federal Income Tax reflects a credit balance of 35% of the debit balance in Account 186.28. When Account 283.28 is credited, Account 410.10 –

Deferred FIT Expense in debited. When Account 283.28 is debited, Account 411.10 – Deferred FIT Expense Credit is credited.

Q. Please explain how retail loads effect power supply costs.

A. Increased retail loads result in increased power supply costs. Likewise, reduced retail loads result in reduced power supply costs.

Q. What causes retail loads to fluctuate?

A. Authorized, weather normalized, retail loads are based on the 1998 test year utilized in the Company's last general rate case, Docket No. UE-991606. The addition of new customers since 1998 has caused retail loads to increase. Colder than normal winter weather and warmer than normal summer weather result in increased retail loads. Conservation, warmer than normal winter weather, and cooler than normal summer weather result in reduced retail loads.

Q. Please explain why the revenue adjustment for the difference between actual and authorized retail revenue included in the current power cost deferral mechanism is appropriate.

A. The current deferral mechanism was amended by Order Granting Request to Modify Power Cost Deferral Mechanism issued January 24, 2001 in Docket No. UE-000972. The modifications to the deferral mechanism, including the retail revenue adjustment, were effective December 1, 2000. Since actual retail load requirements are one of the components that determine actual power supply revenues and expenses, it is appropriate to include a retail revenue adjustment for the difference between actual and authorized revenue in the power cost deferral mechanism. The retail revenue adjustment is included to reflect the difference between actual and authorized retail revenue, adjusted for distribution costs to serve load growth.

Q. Why isn't it appropriate to include the entire difference between actual and authorized retail revenue?

A. Since the Company incurs additional costs to serve new retail load, it is not appropriate to reflect the entire amount of difference between actual and authorized retail revenue in the deferral mechanism, because a portion of increased retail revenue, due to load growth, is offset by increased delivery costs to serve new load. The Company includes a distribution cost adjustment to retail revenue based on increases in customers by rate schedule. The difference between actual customers and authorized customers is multiplied by distribution costs per customer from the Company's last cost of service study to arrive at the distribution cost adjustment.

If the difference between actual and authorized retail revenue is an increase, then that increase adjusted for distribution costs to serve load growth is used to offset increased power supply costs resulting from serving increased retail loads. Likewise, if the difference between actual and authorized retail revenue is a decrease, then that decrease adjusted for distribution costs to serve load growth is used to offset reduced power supply costs resulting from serving reduced retail loads. It should be noted that even though the total difference in retail revenue for a month may be a decrease, the difference in retail revenue due to new customer load growth is always an increase. The adjustment for distribution costs is an offset to the increase in retail revenue due to new customer load growth.

Q. How is the increase or decrease in retail revenue measured?

A. Actual billed retail revenues plus estimated net unbilled revenues for the month are compared against revenues from the Company's last rate case, Docket No. UE-991606. Revenue associated with distribution costs related to load growth is subtracted from the change in revenue. The balance of the change in retail revenue is used to offset the changes in power supply costs. A diagram that illustrates the retail revenue adjustment is identified as Exhibit No.___ (RLM-1). In addition, the monthly reports submitted to the Commission include workpapers showing the calculation of the retail revenue adjustment.

Q. Was a cost of service study used to calculate the distribution cost per customer used in the retail revenue adjustment?

A. Yes. Avista's cost of service study filed in the last case was used to determine the distribution cost per customer in the retail revenue adjustment. The study was updated to include all Commission ordered adjustments and compliance revenues.

Q. Was the Company's cost of service study related to distribution costs approved by the Commission in its last general rate case?

A. No. However, as no alternative method was recommended in the rate case, the Company has used the distribution costs from its study, rerun for Commission ordered revenues and changes to results of operations, to arrive at a reasonable estimate of distribution costs to serve load growth. The Company believes that its calculation presents a reasonable approximation of the distribution costs associated with incremental customers.

Q. What is the total amount of the retail revenue adjustments for the months of December 2000 through September 2001?

A. The retail revenue adjustment has been part of the deferral mechanism since December 1, 2000, when the mechanism was modified. The retail revenue adjustments have resulted in a $6,773,353 offset to deferred power costs for the period December 2000 through September 2001.

Q. Would you please summarize the retail revenue adjustment?

A. Yes. Changes in retail revenues, related to the levels of customers in the last general rate case, are used in their entirety as an offset to changes in power costs. The increase in revenue due to the addition of customers since the last rate case minus an adjustment for distribution costs to serve the additional customers is also used to offset changes in power costs. Retail revenue adjustments have reduced the deferral balance by $6,773,353 for the period December 2000 through September 2001.

Q. Does this conclude your direct testimony?

A. Yes, it does.